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FM AMCONSUL MUMBAI
TO RUEHC/SECSTATE WASHDC PRIORITY 6807
INFO RUEHNE/AMEMBASSY NEW DELHI PRIORITY 8048
RUEHCG/AMCONSUL CHENNAI PRIORITY 1979
RUEHNEH/AMCONSUL HYDERABAD PRIORITY 0011
RUEHCI/AMCONSUL KOLKATA PRIORITY 1774
RUCNCLS/ALL SOUTH AND CENTRAL ASIA COLLECTIVE
RUEATRS/DEPT OF TREASURY WASHINGTON DC
RUCPDOG/DEPT OF COMMERCE WASHINGTON DC
RUEHRC/DEPT OF AGRICULTURE WASHINGTON DC
RUEAIIA/CIA WASHDC
RHEHAAA/NSC WASHINGTON DC
RUEHBI/AMCONSUL MUMBAI PRIORITY 1972

UNCLAS SECTION 01 OF 03 MUMBAI 000573

SENSITIVE
SIPDIS

DEPT PASS TO EXPORT-IMPORT BANK FOR JESSICA FARMER
DEPT PLEASE PASS TO USTR AADLER/CLILIENTFELD

E.O. 12958: N/A

TAGS: [ECON](#) [EFIN](#) [EIND](#) [ETRD](#) [IN](#)

SUBJECT: INDIAN ECONOMY REELING FROM EFFECTS OF FINANCIAL CRISIS, NOT
TERROR ATTACKS

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11. (SBU) Summary. Market participants and corporate representatives tell Congenoffs that the Mumbai terrorist attacks may have a modest, short-term impact on markets and economic activity, exacerbating the more serious and ongoing deterioration of market conditions due to the global economic crisis. Characterizing the current business climate as "bleak," interlocutors pointed to alarming declines in exports and consumer spending in November 2008 as signs of a major economic slowdown. Corporate India also displayed immense anger at the country's political class and have called for security reforms. Though they judged the chances of war with Pakistan as low, they considered this the worst possible outcome. However, NASSCOM remained optimistic, stating that India has a cost competitive advantage that would continue despite the financial crisis or the terror attacks. End Summary.

Terror Attacks Will Depress Weak Economy in the Short-Term

12. (SBU) Interlocutors in Mumbai largely agreed that while the terrorist attacks might have a short-term impact on economic activity, the larger, ongoing economic slowdown in India, caused by the global financial crisis, was far more significant. Ritu Kochchar, Director for Equities for JP Morgan, believes that the attacks will dampen investor sentiment, but notes that foreign investment in India was already waning, as foreign investors had ended their focus on emerging markets, and stopped scouting for deals in October-November 2008. Tushar Poddar, Chief Economist of Goldman Sachs, believes that the attacks will have an immediate impact on third order activity, such as hotels, tourism, and travel, but that the economy was already slowing considerably. Anu Madgavkar, Partner of McKinsey & Co, agreed, but pointed out that the Indian economy was not dependent on these sectors. She believes that the Mumbai economy would temporarily dip but would bounce back soon. Madhav Bhatkuly, Director of New Horizons Investments, believes that business meetings will be postponed following the attacks, which in turn, will lead to the postponement of economic activity in the short-term. For example, he said that four current or potential foreign investors had already postponed business meetings with him.

13. (U) Madgavkar said that the threat of war with Pakistan

will hurt investor sentiment and business the most. However, she believes that India's leaders would not let this happen. Kochchar said foreign investors are worried about an Indo-Pak conflict and political risk in general. Investors are uncertain about the Indian government's next moves, although they expect a focus on security rather than economic reform, particularly since inflation figures are declining. Poddar said that a possible Indo-Pak standoff will hurt the currency. During the 2001-02 standoff with Pakistan following the terrorist attacks on the Indian Parliament, the Indian currency depreciated, prompting RBI intervention. Unlike the present situation, there was no financial crisis in 2001-02, so the impact this time could be worse, he concluded.

Global Financial Crisis Continues to Cause Indian Slowdown

¶4. (SBU) Poddar said that business activity declined significantly in October-November 2008. Bhatkuly concurred, characterizing November 2008 as the worst month that he had ever seen in 16 years of watching corporate India. In a review of 200 Indian companies in which his company has an ongoing or potential investment, Bhatkuly concluded that Indian industrial activity contracted significantly in November 2008. He singled out the auto component segment as experiencing serious stress due to the global contraction of car sales. In addition, companies engaged in the commodities business like Hindalco are in difficult straits, as are highly levered companies like those in the real estate sector. While Indian banks have withstood the global financial crisis, they will soon start to see a rise in non-performing loans, albeit not to alarming levels, he continued. Vikram Shroff, Executive Director of agro-chemicals company United Phosphorus, stated that his company, as an agricultural-related business, has not been too badly hit by the global financial crisis and the U.S. recession. Nevertheless,

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he said that his company had halted expansion and is conserving cash. He pointed out that United Phosphorus made five acquisitions in the first half of 2008, but none in the second half of the year.

¶5. (U) Mohan Nihalani, the President of the All India Importers & Exporters Association, noted that Indian exporters are facing "tough times" as their export orders have either declined or are not being honored. (Note: Exports declined by 12.1 percent in November 2008 as compared to November 2007, marking the sharpest yearly fall in 10 years. End Note.) There has been a significant decline of export cargo loaded at India's largest container terminal port, the Jawaharlal Nehru port, he added. He applauded the government's proposal to award concessions to exporters, such as the refund of service tax and excise duties and the extension of lines of credit as part of the financial stimulus package for the economy. But, Nihalani points out, "the government cannot generate export orders." In a separate discussion, Muffadalal Yusuf of Tajir, a company which imports almonds from the U.S. for processing and sales in India, reported that he had received no new orders for almonds in November 2008.

Financial Crisis and Terror Attacks Cannot Defuse India's Cost Competitive Advantage

¶6. (U) Rajiv Vaishnav, the Regional Director of the National Association of Software & Services Companies (NASSCOM), admitted that the mood in the economy -- hit by the global financial crisis, the recession in the U.S. and now the Mumbai terror attacks -- is low at present, but argued that the Indian industry's cost competitive advantage will enable the economy to withstand these shocks. NASCCOM has earlier revised its export growth forecast for the IT sector for 2008-09 from 29 percent to 21-24 percent. Vaishnav said that this may be further lowered to 20 percent. However, he believes that the slowdown in growth is "temporary" and the mid-term or long-term looks bright, especially for IT software and services. According to Vaishnav,

companies increase outsourcing and off-shoring during economic crises as cost competitiveness becomes central to doing business. Right now, orders are delayed and business decisions are being deferred resulting in the slowdown in the growth of IT exports. But once companies re-commence business operations, they will choose the low cost option. Meanwhile, Indian IT companies are streamlining their operations and gearing up to cater to future needs. They are focusing on innovation and customer servicing and attrition has gone down. The silver lining to the current gloomy economic scenario is that Indian companies are improving their productivity and efficiency, he said. Rit Desai, Assistant Manager (International Marketing) of Larsen & Toubro, agreed with Vaishnav and added that while the Mumbai terror attacks will always be "at the back of the mind" of potential investors, there is no denying India's cost competitiveness in specific sectors. Foreign investors cannot afford to ignore India, he argued.

17. (SBU) Bhatkuly also pointed out some pockets of growth in the economy. He noted that the hike in salary levels of public-sector employees will boost consumption. The loan waiver to farmers has helped the rural economy, but he pointed out, this will still not compensate for the problems in the industrial sector. Another bright spot that he noted was that Alok Industries, a fabric exporting company, was seeing an uptick in orders; this was a result of the vendor consolidation on the part of large global retailers like Wal-Mart, which was shutting down business with marginal suppliers and giving more business to larger suppliers. He acknowledged that this would not help small and medium enterprises in this business.

Mumbai Attacks Not a Factor in Market Activity

18. (U) After remaining closed the first day after the attacks, the Bombay Stock Exchange's SENSEX - a barometer for Indian stock market performance -- closed up one percent when it re-opened on Friday, November 28, while anti-terrorist operations were on-going. However, on December 1, markets

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dropped three percent, in reaction to declines in the U.S. and Asia, as well as negative information on exports and auto sales in India. According to market participants, three key factors cushioned the Indian markets from the impact of the terrorist attack. First, India's unfortunate familiarity with terrorism means that markets have grown accustomed to these tragedies, and react modestly, if at all. Second, markets have anticipated an RBI rate cut, and these attacks have raised expectations for further economic relief. Third, with an over 50 percent decline in the SENSEX since January, and the deterioration of credit markets, there wasn't much room to fall. External credit markets are already prohibitively expensive, commercial paper markets blocked, and investment plans on hold.

Shocked and Angered Corporate Mumbai Blames the Political Class

19. (SBU) Rajiv Lall, the Managing Director of Infrastructure Development Finance Corporation, stated that India was facing a crisis of governance. He condemned the failure to protect Mumbai's residents as being emblematic of the politicians' failure to build or maintain India's decaying institutions. United Phosphorus' Shroff said that bad governance in India is the reason why the majority of Indians working overseas do so well, while the majority of Indians in India barely survive. Madgavkar was saddened that she could not expect much out the current group of leaders running India and the state of Maharashtra.

110. (SBU) Bhatkuly was disappointed with the economic reforms of the Congress-led United Progressive Alliance (UPA) government but was even more unhappy with its neglect of security. While not a fan of the rival Bharatiya Janata Party (BJP) either, Bhatkuly believes that the BJP was more pro-active in office, and initiated economic reforms earlier this decade that enabled

the Indian economy to grow. During the past four years of the UPA-government's rule, India was awash with excess liquidity that was sweeping the globe. Bhatkuly believes that this inflated India's growth rate and allowed the economy to surge without reforms. Even easy reforms which no one would oppose or object to -- like unclogging the nation's courts - were not carried out. Instead, he added, the reform process has moved backwards. He pointed to the Finance Minister's statements asking the Reserve Bank of India (RBI) to cut interest rates; the central bank responded by taking this action the next day, bringing the independence of the RBI into question.

¶11. (SBU) Pradeep Bhargava, Managing Director of Cummins Generator Technologies and Head of the Maharashtra Council of the Confederation of Indian Industries (CII), said that CII is planning to push the federal government to implement internal security reforms, including establishing a single coordinating agency to respond and defend against terror attacks. CII spokespersons are also trying to boost investor sentiment and restore confidence in investing in India, but Bhargava believes that instead of meaningless platitudes, it would be more effective if foreign investors can see improved security measures in place to protect the country against senseless terrorist attacks.

¶12. (SBU) Comment: In the past, many corporate leaders have told Congenoffs that India grows despite the government, not because of it. Business contacts agree that the impact of the attacks will be mild, but will exacerbate a longer term decline in sentiment and activity caused by the global financial crisis. However, corporate leaders in Mumbai are shaken by the attacks, and angry at the inability of their government to prevent them.

The Indian government is likely to announce new measures to help Indian industry through the financial crisis, but it may take longer to relieve the public desire for deep reform. Perhaps, even corporate India has reached the end of its hands-off approach to the country's political class and governance. The alternative - especially in neglected, misgoverned Mumbai - is not clear. End Comment.

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